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PANAMA
CURRENT ECONOMIC SITUATION AND SHORT-TERM OUTLOOK

GENERAL

1. Panama's economy, while still the strongest in Central America, has been less dynamic in the 1970s than in the 1960s. Economic growth in 1974 shows signs of slowing still further. Private investment appears to have weakened in the first half, and exports have been sluggish. Higher oil prices and rising unemployment probably have slackened the growth of real consumption expenditure, although general wage increases adopted in May and June may have prompted partial revival. In the first half, real GDP growth at the annual rate probably fell significantly below 1973's 6.5%.

2. The economy's slowdown this year appears to derive largely from business uncertainty created by soaring interest rates and the impact of worldwide inflation on import costs. At the end of the first quarter of 1974, wholesale prices in Panama were 29% higher than a year earlier, almost entirely the result of increased import prices. In Panama District, where more than 30% of economic activity is located, for example, higher interest rates and prices evidently helped to sharply discourage new

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investment projects, cutting the value of construction in the first six months to 60% of that in the same period of 1973.

FISCAL POSITION

3. The government's financial situation has deteriorated thus far in 1974. This contrasts sharply with last year when stringent economy measures enabled Panama to achieve the smallest current account budget deficit since 1966. In the first half, higher material prices and unplanned expenditures such as for government wage increases have created a sizable current deficit and, together with a doubling of public investment outlays from last year, have greatly increased the overall deficit.

4. The overall deficit this year is being financed mainly with long-term borrowing from commercial banks at high interest rates. Drawings thus far have exceeded \$35 million. The government's financial position nevertheless remains much stronger than in the early years of the Torrijos regime. The strengthening has resulted from refinancing of the large short-term debt during the last several years, greatly reducing the debt service burden.

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TRADE AND PAYMENTS DEVELOPMENTS

5. Soaring import prices and sluggish exports are expected to boost Panama's chronic trade deficit by 25% - 30% in 1974. The rise would have been even greater had not part of the impact of higher crude oil prices been offset by raising prices charged for petroleum products that Panama exports or sells as bunker fuels. Despite increased service receipts from transactions with the Canal Zone and the Colon Free Zone, the current account deficit probably will rise by nearly the same proportion. The deficit, normally covered mainly by government long-term borrowing, should nevertheless remain manageable.

SHORT-TERM OUTLOOK

6. Economic growth probably will remain sluggish during the remainder of 1974. Since high interest rates and rapid price gains undoubtedly will persist, private investment is likely to remain depressed. The Torrijos government unquestionably would like to further accelerate public investment this year to compensate for weak private outlays. Because of limits to government borrowing capacity, however, it is unlikely to be able to do so.

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7. Prospects for the next several years are brighter, although the economy may well fail to recover the buoyancy of the 1960s. Much depends on how Panama fares economically from the Treaty negotiations. The growth of income from the sale of services to the Canal Zone has slowed in recent years. This has tended to reduce opportunities for investments to expand production for the domestic market, which accounted for much of the earlier dynamism. At the same time, Panama's narrow resource base severely limits the possibilities for export expansion. While the country has sizable commercial copper deposits, market uncertainties and apparent lack of confidence in the Torrijos government have delayed their exploitation. Without greatly increased Canal revenues, there seems to be little chance that public investment can be expanded enough to provide real economic impetus: future government revenues have already been heavily mortgaged to meet past public investment needs.

CIA/OER
27 September 1974

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MEMORANDUM FOR THE RECORD

SUBJECT: Panama: Current Economic Assessment

The attached assessment of the Panama economy has
been forwarded to [redacted] Assistant National
Intelligence Officer for Latin America, [redacted]

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Attachment:
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